APPLIED ECONOMICS

MARICOPA ASSOCIATION OF GOVERNMENTS
GROWING SMARTER IMPLEMENTATION:
HISTORIC SALES TAX BASE

FINAL REPORT

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1.0 INTRODUCTION

This paper is one of a series on regional technical reports that are funded under a grant by the Federal Highways Administration for MAG's Regional Growing Smarter Implementation Project. There are 13 regional technical reports in four categories:

1. Growth reports – (1) Demographic & Social Change; and (2) Economic Change
2. Distribution – land use, real estate, and socioeconomics
3. Infrastructure reports – (1) Water Supply; (2) Regional Transportation Systems; (3) Regional Water/Wastewater Treatment; (4) Regional Open Space; (5) School Facilities; and (6) Cost of Regional Infrastructure
4. Regional issues reports – (1) Sales Tax Base; (2) Fiscal Balance; (3) Affordable Housing; and (4) Commute Sheds

This report presents the results of a regional issues report on Sales Tax Base. The goal of this task is to provide a general understanding of the role of retail development in Maricopa County and the importance of sales tax revenue to local MAG member agencies.

Sales tax collections are an important generator of local revenue, and place municipalities in a competitive situation for land uses and development that generate sales tax revenues. Though this report was written prior to the effect of the September 11 terrorist attack, it has since become clear that the State and its municipalities are exceptionally dependent on sales taxes. Additionally, both the State and the Metro Phoenix economy are highly dependent on consumer purchases, which make us highly vulnerable to recessionary downturns in construction, retail sales, and tourism.

This report examines the sales tax rates and structure in Maricopa County municipalities. Additionally, it examines long-term trends in retail market conditions that will have a significant impact on future fiscal conditions in the metropolitan Phoenix area. This report can be used as a reference tool for local planning and development.

- Chapter 2 presents the relative importance of sales tax revenue to the jurisdictions;
- Chapter 3 reviews the sales tax collections by industry for each jurisdiction;
- Chapter 4 discusses national and local retail industry trends; and
- Chapter 5 examines the current level of tourism and related expenditures in both Arizona and Maricopa County, since tourism is a major element of the regional economic base.

2.0 LOCAL SALES TAX REVENUE

Sales tax revenues are a major source of funding for municipal and county governments in Arizona and Metro Phoenix. Local jurisdictions receive a variety of types of revenues; some of which are generated locally and some that are distributed by other levels of government. Some of these revenues are assigned to a specific fund and are restricted for certain types of expenditures, while other revenues, mainly in the general fund, are unrestricted. Typically, local sales tax revenues are unrestricted, although many cities have tax overrides to fund special programs. This chapter discusses the importance of sales tax as a locally controlled revenue source for cities.

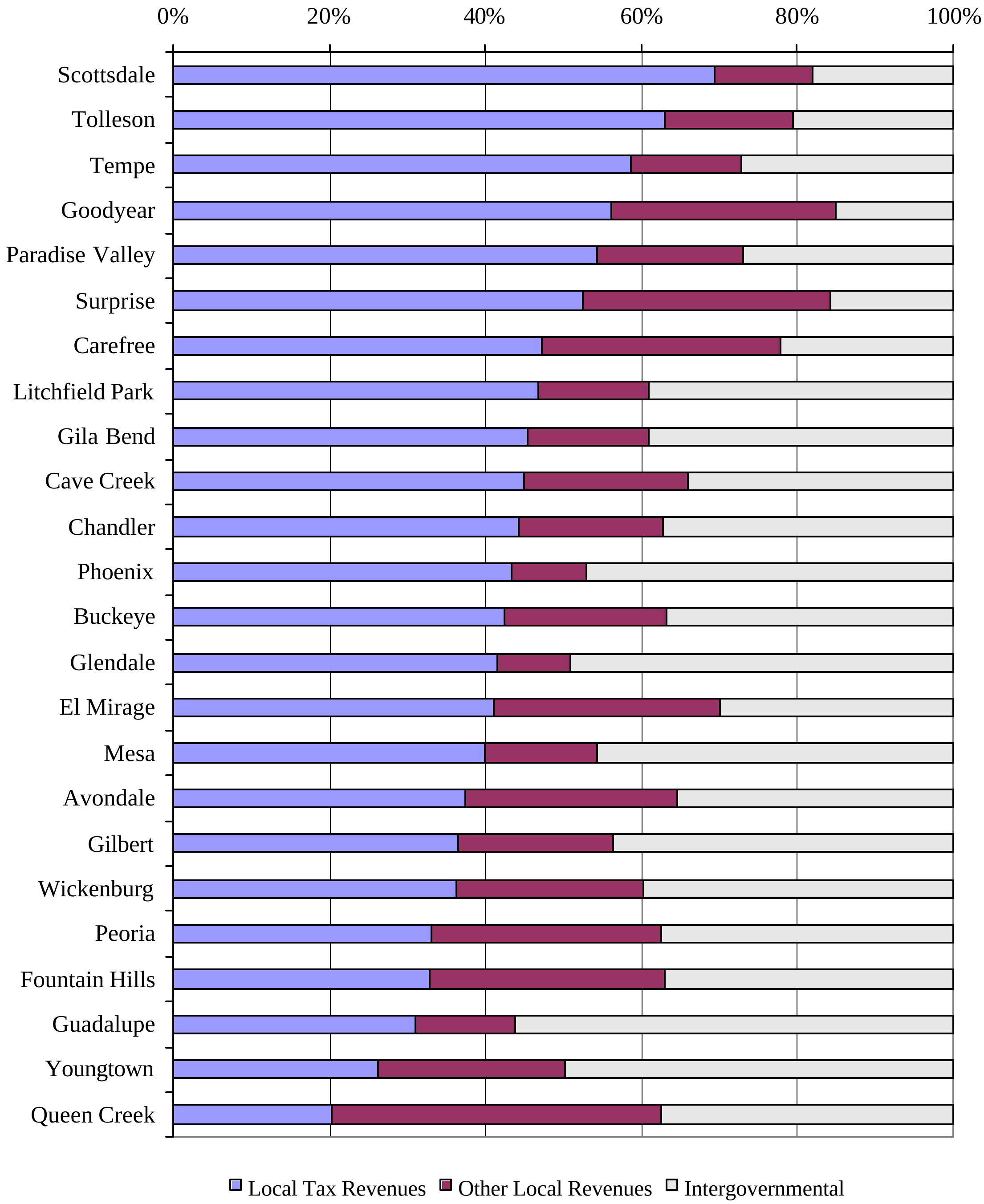
2.1 Sources of Local Operating Revenue

Locally controlled revenue sources include sales and property taxes, fines, licenses, permits and rents. Most of these revenues are unrestricted in nature, meaning they can be used in the general fund to cover a variety of expenditures. In Arizona, non-local revenue sources for cities include intergovernmental funds and grants. Most of the intergovernmental revenues are also unrestricted in nature, although some are designated for transportation expenditures. Unrestricted general fund revenues include state-shared sales and income tax, which are distributed based on population. While the proportions vary across the jurisdictions, on average locally generated revenues constitute approximately 61 percent of the operating budgets in the jurisdictions in Maricopa County.

There are two broad categories of locally generated revenues included in operating budgets - taxes and non-tax revenues. The former category includes property, sales and special sales taxes. Other non-tax revenues may include fees, service charges, permits, licenses, rents and interest. Figure 2-1 shows the composition of operating revenues for cities in Maricopa County. Revenue types include local taxes, other local revenues and intergovernmental revenues and grants. *Local taxes account for the majority of general fund resources. This is especially true in cities with higher tax rates and significant sales and/or property tax bases* including Phoenix, Scottsdale, Tempe, Glendale and Litchfield Park. Only in a handful of municipalities such as Peoria, Youngtown, Queen Creek and Fountain Hills do tax collections account for less than 55 percent of the locally generated revenues. With the exception of Peoria, none of these four cities with a lower level of local tax collections collects local property taxes.

Note that *there is no clear correlation between the size or location of the municipality and the breakdown of operating fund revenues by type.* For example, the small rural town of Wickenburg has a structure more similar to that of Gilbert, than that of Goodyear, a smaller more similar community. *Factors that do affect the composition of general fund resources include the local sales and property tax rates, which vary across jurisdictions.* The basic general fund sales tax rates vary from 1 to 3 percent, and local property tax rates vary from 0.0 to 1.64 percent. In jurisdictions with higher tax rates and property and sales values, such as Tempe and Scottsdale, the amount of revenue generated by local tax collections accounts for a greater share of revenues. Conversely, local taxes generate a smaller share of revenues in Guadalupe and Youngtown, which have little taxable economic activity and no local property tax.

FIGURE 2-1
SHARE OF OPERATING REVENUES BY TYPE
MARICOPA COUNTY MUNICIPALITIES



Sources: City Budgets, 1999-00, 2000-01; Applied Economics, 2001.

2.2 Overall Sales Tax Collections

Less than half of the municipalities in Maricopa County levy a local property tax while all municipalities collect sales tax. Sales tax is the largest source of locally generated revenue in all the jurisdictions except Queen Creek, which has little to no retail development. *Not only is sales tax the main source of revenue in terms of local tax collections, but it often the largest single source of revenue in the general fund.* For this particular comparison, sales tax includes the general sales tax, transient occupancy tax and utility tax. While the county does levy its own sales tax, it is not considered in this analysis since all county sales tax is earmarked for special purposes, and not the general fund.

Sales tax accounts for between 20 and 55 percent of most cities' operating budgets (Figures 2-2 and 2-3). The average and median shares for the 24 municipalities are 40 and 39 percent, respectively. The cities with the lowest dependence on sales taxes are Queen Creek and Youngtown, which only have a small amount of retail activity. Among the large cities, Tempe has the highest share while Phoenix has the lowest share, even below the average for all cities. This is likely the result of different revenue structures in the two cities. Phoenix generates a much higher share of general fund revenues from property taxes and intergovernmental revenues than Tempe, due to the greater land area and larger population.

The data presented in this analysis are derived from 24 unique city and town budgets. Just as tax structures and rates are not equal across the jurisdictions, neither is the manner in which each city presents its annual budget. For example, some cities may not include separate line items for sales tax generated by utilities or by transient lodging.

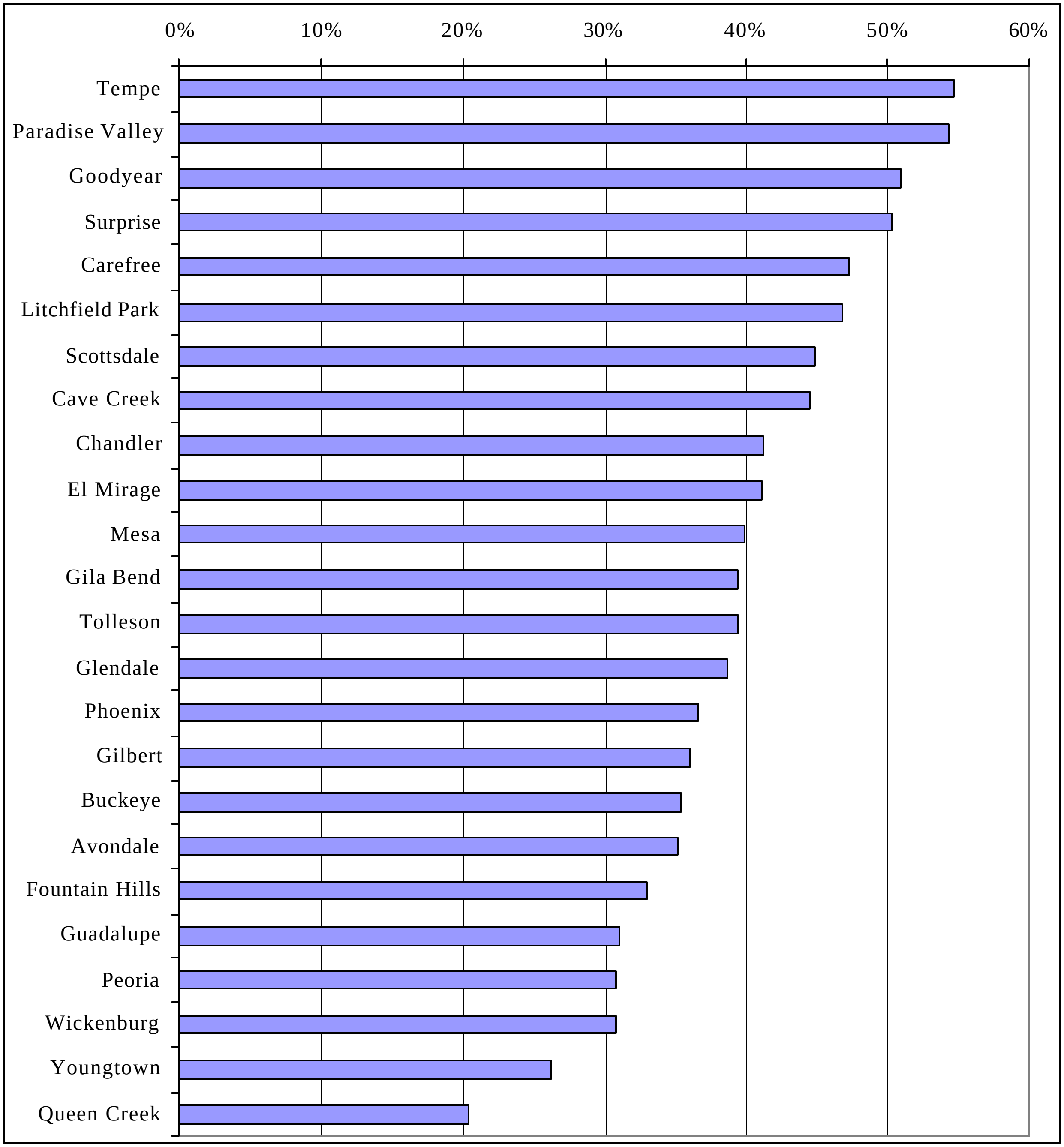
It is important to note that this analysis considers only the sales tax collected in the general fund; however, some cities impose additional sales tax for specific expenditures. For instance, the City of Phoenix currently levies a half-cent sales tax for the funding of the light rail. While this tax may represent an increased sales tax burden to consumers, the sales tax does not directly affect local operating budgets, since the funds are designated for a separate purpose. Similarly, the City of Scottsdale currently has a sales tax override for the funding of transportation improvements, land preservation and tourism promotion. While this does not specifically affect the general fund, the overall local sales tax collected may be higher than the figures here indicate. It can be argued that even though the increased amount of local sales tax is specified for a certain spending measure, these restricted revenues are substituted for general fund revenues, freeing them up for other uses. Regardless of the destination of the revenues, sales tax plays an extremely important role in local funding.

FIGURE 2-2
SALES TAXES AS PERCENT
OF LOCAL OPERATING REVENUE

City/Town	Share	City/Town	Share
Tempe	55%	Tolleson	39%
Paradise Valley	54%	Glendale	39%
Goodyear	51%	Phoenix	37%
Surprise	50%	Gilbert	36%
Carefree	47%	Buckeye	35%
Litchfield Park	47%	Avondale	35%
Scottsdale	45%	Fountain Hills	33%
Cave Creek	44%	Guadalupe	31%
Chandler	41%	Peoria	31%
El Mirage	41%	Wickenburg	31%
Mesa	40%	Youngtown	26%
Gila Bend	39%	Queen Creek	20%

Sources: City Budgets, 1999-00, 2000-01; Applied Economics, 2001.

FIGURE 2-3
SALES TAXES AS PERCENT
OF LOCAL OPERATING REVENUE



Sources: City Budgets, 1999-00, 2000-01; Applied Economics, 2001.

*The general fund does not include enterprise funds

2.3 Sales Tax Collections per Capita

At the local level, the per capita sales tax collections by jurisdiction vary throughout Maricopa County (Figure 2-4). Total retail sales collections are shown on a per capita basis since population generally drives retail sales.

Overall, retail sales tax collections per capita across jurisdictions average $159, although there is a great deal of variation. For example, Scottsdale has a high level of tourism activity; therefore its retail sales per capita are higher because of non-resident sales. Tempe has elevated sales per capita due to tourism, major sporting events and purchases by Arizona State University students. The very low per capita rates for Litchfield Park and Paradise Valley reflect the limited amount of non-tourist retail development in those cities. Low retail tax collections per capita may indicate potential for future growth in emerging peripheral jurisdictions like Queen Creek, El Mirage and Surprise.

FIGURE 2-4
COMPARATIVE SALES TAX COLLECTIONS
MARICOPA COUNTY

	Retail Tax per Capita	Population
Tempe	$358.09	158,625
Scottsdale	$293.75	202,705
Tolleson	$247.06	4,690
Goodyear	$215.02	18,911
Gila Bend	$192.56	1,980
Mesa	$173.17	396,375
Carefree	$172.87	2,927
Cave Creek	$160.23	3,728
Wickenburg	$144.37	5,175
Phoenix	$139.48	1,321,045
Chandler	$129.06	176,581
Glendale	$127.26	218,812
Peoria	$119.92	108,364
Avondale	$113.26	35,883
Surprise	$70.83	30,848
Gilbert	$68.83	109,697
Buckeye	$68.65	6,537
Fountain Hills	$59.43	20,235
Guadalupe	$49.13	5,228
El Mirage	$44.55	9,910
Youngtown	$38.57	3,010
Queen Creek	$30.89	4,316
Paradise Valley	$14.07	13,664
Litchfield Park	$13.67	3,810
Average	$159.61	

Sources: Arizona Department of Revenue; City of Phoenix; City of Chandler; City of Mesa; City of Tempe; City of Avondale; City of Peoria; City of Scottsdale; City of Glendale; Applied Economics, 2001.

2.4 Retail Sales per Capita in Comparative Metro Areas

Given that the majority of taxable sales come from retail establishments, a brief examination of retail activity in Maricopa County compared to other metropolitan areas *of comparable size* provides a useful frame of reference. Figure 2-5 shows retail sales activity and per capita sales as reported by Woods and Poole, a national economic forecasting firm. It should be noted that these figures should not be compared with the local retail sales tax per capita, because the data presented in Figure 2-5 only indicate the total retail sales, not tax collections, which vary depending on tax rates and structures.

FIGURE 2-5
RETAIL SALES PER CAPITA
METROPOLITAN STATISTICAL AREAS

MSA		Total Retail Sales (000)	Population (000)		Retail Sales per Capita
Atlanta, GA	$	50,328,640	3,987.55	$	12,621
Baltimore, MD	$	25,644,040	2,533.19	$	10,123
Cleveland, OH	$	23,574,860	2,224.02	$	10,600
Dallas, TX	$	41,057,730	3,385.34	$	12,128
Denver, CO	$	25,867,930	2,036.41	$	12,703
Houston, TX	$	43,682,960	4,138.52	$	10,555
Maricopa County	**$**	**36,520,780**	**2,998.78**	**$**	**12,179**
Miami, FL	$	24,941,020	2,218.81	$	11,241
Minneapolis, MN	$	36,737,910	2,947.15	$	12,466
Orange County, CA	$	32,502,950	2,843.97	$	11,429
Pittsburgh, PA	$	24,128,200	2,333.20	$	10,341
Portland, OR	$	23,140,680	1,911.93	$	12,103
St. Louis, MO	$	27,641,770	2,593.36	$	10,659
San Diego, CA	$	27,884,910	2,913.07	$	9,572
San Jose, CA	$	20,112,000	1,676.21	$	11,998
Seattle, WA	$	31,308,440	2,397.20	$	13,060
Tampa, FL	$	28,837,770	2,330.09	$	12,376
Average				$	11,522

Source: Woods and Poole, "The Complete Economic and Demographic Data Source", 2001.

Retail sales per capita in Maricopa County are above the average for the comparable metro areas in terms of retail sales taxes per capita. *Maricopa County is fourth highest among comparably sized regions behind only Seattle, Tampa, and Atlanta.* This indicates the relative strength of the retail sector in the Phoenix area and the contribution of tourism. Portland, Dallas, San Jose and Tampa are most similar to Phoenix in terms of sales per capita. In spite of the very similar retail sales tax bases, the collections from sales tax in each area may be quite different because of the tax rates and structures. For instance, Portland does not impose state or local sales tax, which means it does not directly benefit from high or low retail sales per capita, as do jurisdictions in Maricopa County. Interestingly, San Diego, which has a tourism base similar to that of Phoenix, is well below average in sales per capita. The relative strength of the local tax base is an indicator of the viability of sales tax as a primary source of local operating revenue.

2.5 State Sales Tax Rates and Collections

State level sales tax rates in the United States can range from 2.9 to 7 percent (Figure 2-6). In most states, these rates are in addition to local sales taxes. Note some states do not impose sales tax and rely on revenues from other sources, such as income or property tax. The State of Arizona imposes the rate of 5.6 percent, which is slightly above the median tax rate of 5.0% for the nation. The state sales tax is the basic rate charged on general sales in Arizona; however, alternative tax rates apply for certain business activities.

Revenue generated from state imposed sales tax directly benefits municipalities in Arizona, and most other states, through revenue sharing. Therefore, these state revenues increase the positive impact of a viable tax base on municipal budgets. Due to the equalized nature of state revenue sharing, state sales taxes are especially important for cities with limited local retail development.

FIGURE 2-6
STATE SALES TAX RATES
JANUARY 2001

State	Tax Rate	State	Tax Rate
Mississippi	7.00%	New Mexico	5.00%
Rhode Island	7.00%	North Dakota	5.00%
Minnesota	6.50%	Ohio	5.00%
Nevada	6.50%	South Carolina	5.00%
Washington	6.50%	Vermont	5.00%
Illinois	6.25%	Wisconsin	5.00%
Texas	6.25%	Kansas	4.90%
Connecticut	6.00%	Utah	4.75%
Florida	6.00%	Oklahoma	4.50%
Kentucky	6.00%	Missouri	4.23%
Michigan	6.00%	Alabama	4.00%
New Jersey	6.00%	Georgia	4.00%
Pennsylvania	6.00%	Hawaii	4.00%
Tennessee	6.00%	Louisiana	4.00%
West Virginia	6.00%	New York	4.00%
California	5.75%	North Carolina	4.00%
District of Columbia	5.75%	South Dakota	4.00%
Arizona	**5.60%**	Wyoming	4.00%
Arkansas	5.13%	Virginia	3.50%
Idaho	5.00%	Colorado	2.90%
Indiana	5.00%	Alaska	0.00%
Iowa	5.00%	Delaware	0.00%
Maine	5.00%	Montana	0.00%
Maryland	5.00%	New Hampshire	0.00%
Massachusetts	5.00%	Oregon	0.00%
Nebraska	5.00%		
		U.S. Median	5.00%

Source: Federation of Tax Administrators, 2001.

Tax rates, retail sales activity and the size of the local population are all factors that help determine the per capita contribution of sales tax collections (Figure 2-7). Statewide sales tax collections range from as little as $327 to over $1,200 per resident throughout the 50 states. As would be expected, there are some states that show a direct correlation between tax rates and per capita sales tax collections. Washington, Nevada, Florida and Connecticut are among the top five in per capita collections and each has sales tax rate of 6 percent or higher. Likewise Virginia, Alabama and Colorado have very low per capita collections that likely reflect the low state sales tax rates. *Arizona ranks 13th in per capita collections*, a reflection of both a slightly above average sales tax rate as well as strong retail and tourism activity.

This trend is not necessarily the rule for all state sales tax collections. Despite low tax rates in Hawaii, Wyoming and New Mexico, the per capita collection is well above the median. This is likely due to relatively smaller resident populations in these states, combined with a significant presence of non-retail revenue generating activities. Similarly, high tax rates do not always translate into large per capita collections as noted in Rhode Island (7 percent), Illinois (6.25 percent) and West Virginia (6 percent), where sales tax collections per capita are well below the median.

FIGURE 2-7
GENERAL SALES TAX COLLECTIONS PER CAPITA AND AS A PERCENT OF TOTAL REVENUE

State	Per Capita	% of Total	State	Per Capita	% of Total
Washington	$1,214.43	24.69%	Idaho	$531.34	13.88%
Hawaii	$1,194.76	21.08%	Pennsylvania	$526.02	13.02%
Nevada	$948.39	22.63%	Georgia	$522.56	15.53%
Connecticut	$925.97	18.35%	Kentucky	$503.31	12.39%
Florida	$866.43	24.97%	Ohio	$493.44	11.49%
New Mexico	$837.63	16.06%	North Dakota	$484.36	9.88%
Michigan	$771.38	18.90%	Missouri	$483.19	13.82%
Tennessee	$741.68	24.15%	Massachusetts	$481.94	10.49%
Mississippi	$739.37	19.18%	West Virginia	$471.78	10.97%
Wyoming	$697.40	12.64%	Illinois	$464.58	13.83%
Minnesota	$686.42	13.23%	Louisiana	$453.48	11.25%
Maine	$667.68	14.60%	North Carolina	$433.68	9.82%
Arizona	**$653.32**	18.39%	Maryland	$420.90	10.51%
California	$652.10	14.69%	New York	$419.00	7.92%
Texas	$631.30	21.58%	Oklahoma	$396.90	10.90%
Utah	$624.81	14.97%	Colorado	$385.51	11.33%
Kansas	$615.90	19.18%	Alabama	$360.90	10.58%
South Dakota	$599.52	15.40%	Vermont	$329.17	8.20%
Arkansas	$596.33	15.95%	Virginia	$327.63	8.58%
New Jersey	$587.33	12.88%	New Hampshire	$0.00	0.00%
Wisconsin	$583.40	14.24%	Alaska	$0.00	0.00%
South Carolina	$563.84	14.23%	Delaware	$0.00	0.00%
Nebraska	$553.16	16.32%	Montana	$0.00	0.00%
Indiana	$535.03	17.05%	Oregon	$0.00	0.00%
Iowa	$534.10	15.24%			
Rhode Island	$531.80	11.85%	U.S. Median	$578.15	14.23%

Source: Colorado Public Expenditure Council, "State Taxes and Spending," 2001.

While sales tax collections can represent a major source of both local and state revenues, the dependence on sales tax revenue relative to the per capita collections is an important factor for both local and state governments, since retail sales are subject to economic recessions as well as growth periods. As previously noted, five states that do not impose a general sales tax and therefore sales tax revenues do not figure into state budgets. Of the states that do tax sales, the median share of state sales tax collections as a percent of total state revenue is 14.23 percent. Florida has the highest dependence on sales tax collections, accounting for almost one fourth of its state revenues, while sales taxes compose less than 8 percent of New York's revenues. Among the top 15 states with the highest sales tax collections per capita, the share of the revenues contributed by sales tax is below the median in only two states signaling that the higher tax collections per capita generally correspond to the respective budgetary significance.

Most states return a portion of state collected sales tax directly to cities through revenue sharing. The share that is directly returned to the municipality will vary depending on the state tax and finance structures. *In Arizona, municipalities receive 25 percent of the distribution base of the transaction privilege tax, which is allocated based on the jurisdiction's share of the total population.* The distribution base varies depending on the level of activity and can be as much as 40 percent or as little as zero percent of total state collections. In fiscal year 1999/2000, approximately 8.7 percent of state sales tax collections were returned directly to the cities, while the counties received about 14.1 percent.[1]

Since sales activity and the subsequent local and state collections represent a major source of funding for local jurisdictions, it is important to examine the composition and contribution of sales by industry group in Maricopa County. The following chapter provides more detail as to the level of revenue generation by industry in each jurisdiction, which can be useful when determining future contributions of specific types of development.

[1] Arizona Department of Revenue, "Tax Facts", March 2001.

3.0 SALES TAX GENERATION BY INDUSTRY

Retail establishments are the primary generators of sales taxes, however, many other types of industries contribute to the local tax base. Therefore, it is worthwhile to examine the sales tax contributions by industry in each municipality. The first section of this chapter provides the local sales tax rates of the jurisdictions and the second section presents the collections by industry. The purpose of this analysis is to understand the complexities of sales tax revenue generation by industry across the diverse jurisdictions in Maricopa County.

3.1 Local Sales Tax Rates

While the state sales tax rate is uniform across Arizona, municipalities levy sales taxes of 0 to 3 percent for local funding, although there is no upper limit on sales tax rates. It is important to note that because sales tax rates and structures differ across the jurisdictions and industries, comparisons of the absolute amount of sales tax collected are not always accurate indicators of the exact level of economic activity. Figure 3-1 presents the local tax rates charged on general sales, utilities and lodging. *Note that only a small number of communities impose a higher tax on utilities, while lodging taxes typically exceed the general sales tax rate.*

FIGURE 3-1
LOCAL GENERAL FUND SALES TAX RATES, MARICOPA COUNTY

Jurisdiction	Sales Tax	Utility Tax	Lodging Tax
El Mirage	3.00%	3.00%	5.00%
Gila Bend	3.00%	3.00%	5.00%
Cave Creek	2.50%	3.00%	6.50%
Surprise	2.00%	2.00%	3.00%
Goodyear	2.00%	2.00%	4.00%
Buckeye	2.00%	2.00%	2.00%
Guadalupe	2.00%	2.00%	6.00%
Tolleson	2.00%	2.00%	4.00%
Litchfield Park	2.00%	2.00%	3.00%
Youngtown	2.00%	2.00%	4.00%
Carefree	2.00%	2.00%	5.00%
Phoenix	1.80%	2.70%	4.80%
Tempe	1.80%	1.80%	3.80%
Fountain Hills	1.60%	1.60%	4.60%
Mesa	1.50%	1.50%	4.00%
Chandler	1.50%	2.75%	4.40%
Gilbert	1.50%	1.50%	4.50%
Peoria	1.50%	3.00%	5.00%
Avondale	1.50%	2.00%	3.50%
Scottsdale	1.40%	1.40%	4.40%
Paradise Valley	1.40%	1.40%	4.40%
Glendale	1.30%	1.30%	4.30%
Wickenburg	1.00%	1.00%	1.00%
Queen Creek	1.00%	1.00%	2.00%
Maricopa County	0.00%	0.00%	0.57%

Sources: Arizona Department of Revenue, 2001; City Budgets, 2000.

The lowest local sales tax rate, 1 percent, is found in Wickenburg and Queen Creek, both smaller communities on the periphery of the metropolitan area. El Mirage and Gila Bend, which do not have local property taxes, have the highest sales tax rate of 3 percent. Five municipalities levy an additional sales tax on utilities while almost all municipalities charge an additional lodging or transient occupancy tax, for hotels and short-term lodging providers. The decision to tax certain industries at a higher rate varies depending on revenues generated by other sources. It should be noted that not all retail sales are subject to the same tax rate within certain jurisdictions. For example, some cities tax grocery store food sales while others do not. Likewise, some cities tax higher priced retail items at higher rates[2]. Note that while Maricopa County charges a 0.7 percent sales tax in addition to the city rates, these revenues are used exclusively for jail and transit expenditures and are not part of the county's general fund.

3.2 Sales Tax Collections by Industry

The purpose of this section is to compare the sales tax collection by industry across cities. The Arizona Department of Revenue tracks sales tax collections by industry for municipalities for whom they collect sales tax. However, there are eight municipalities in Maricopa County that collect their own sales tax, and they have their own systems for recording taxes collected by industry. For this analysis, data from each municipality was organized into six uniform industry categories to compare collections by type, however this approach was limited by the detail of the source data (Figure 3-2).

- The retail category includes retail and restaurant sales tax collections.
- The utility category includes transportation, communication, and utility activities.
- Property includes lease tax collections on rental properties.
- A major source of municipal sales taxes is from construction, especially for fast-growing municipalities. The owner of a new home or building must pay sales taxes on all construction. The sales tax is based on the contracted amount for construction – not only materials. The full amount of the contract is taxed, less a 35% deduction for labor.
- Hotel includes sales tax on transient lodging.
- Other includes the remainder of activities for which sales tax is derived including publishing, manufacturing equipment, advertising, printing and other miscellaneous activities.

As a caveat, just as the tax structures and rates of each municipality vary, the categories of taxable sales reported also vary. The eight cities that report sales tax collections individually generally have more precise categories. For example, the City of Chandler records sales tax by 4-digit SIC code (over 250 categories) while Tempe and Peoria report collections in 15 to 16 categories. The Department of Revenue reports collections in eleven industry categories. Although most jurisdictions have hotels and rental properties, many did not report hotel or rental property tax collections under those categories, rather designating them to general retail or other. This is especially true in the case of municipalities where tax collections were reported by the Department of Revenue. The Department of Revenue reports collections based on the industry code listed on the sales tax license, regardless of the type of tax. Therefore, it is possible that some activities, which could more appropriately be designated in different categories, may be listed in a more general category, thus causing some data inconsistencies between cities.

[2] Some tax certain high cost retail items at lower rates, e.g. care dealer exemptions. Some also use differential rates on high cost retail items, e.g. the first $5,000 is taxed at 2% and after $5,000 is taxed at 1%.

FIGURE 3-2
SALES TAX COLLECTIONS BY INDUSTRY
MARICOPA COUNTY

City/Town	Retail	Construction	Utilities	Property	Hotel	Other	Total
Phoenix	$184,253,660	$32,074,075	$61,588,625	$25,637,484	$34,012,580	$45,390,777	$382,957,201
Scottsdale	$59,544,657	$23,006,614	$5,093,047	$11,173,474	$6,218,076	$6,878,979	$111,914,847
Mesa	$68,640,645	$13,031,708	$8,723,518	$11,786,614		$2,024,350	$104,206,835
Tempe	$56,801,901	$6,904,426	$8,685,098	$11,298,216	$3,831,283	$7,916,335	$95,437,259
Chandler	$22,789,260	$10,162,871	$8,762,249	$3,386,833	$1,318,428	$3,719,554	$50,139,195
Glendale	$27,846,791	$4,435,164	$2,187,412	$4,152,559	$153,320	$1,192,123	$39,967,369
Peoria	$12,994,724	$4,429,409	$1,049,220	$1,091,432	$368,366	$421,298	$20,354,449
Gilbert	$7,550,570	$4,053,872	$1,263,604			$2,892,721	$15,760,767
Surprise	$2,184,994	$6,343,376	$635,635		$133,121	$1,183,143	$10,480,269
Goodyear	$4,066,232	$2,401,426	$221,695			$2,140,628	$8,829,981
Avondale	$4,064,231	$2,451,738	$332,474	$329,572		$359,263	$7,537,278
Paradise Valley	$192,222	$1,647,004	$269,824		$3,753,983	$1,561,226	$7,424,259
Fountain Hills	$1,202,570	$1,851,784	$349,713			$628,345	$4,032,412
Tolleson	$1,158,691	$939,476	$406,964			$419,732	$2,924,863
El Mirage	$441,446	$1,753,886	$130,344			$276,694	$2,602,370
Carefree	$505,991	$592,007	$185,551			$621,770	$1,905,320
Cave Creek	$597,325	$408,093	$222,959			$524,473	$1,752,850
Buckeye	$448,788	$511,190	$159,137			$326,724	$1,445,838
Litchfield Park	$52,084	$158,467	$61,970			$951,433	$1,223,954
Wickenburg	$747,089	$104,474	$62,459		$23,910	$135,319	$1,073,251
Guadalupe	$256,840		$194,494			$266,031	$717,364
Gila Bend	$381,267		$148,508			$93,644	$623,419
Queen Creek	$133,331	$211,682	$71,191			$148,449	$564,653
Youngtown	$116,098	$33,115	$26,452			$206,464	$382,128
Total	$456,971,406	$117,505,858	$100,832,144	$68,856,184	$49,813,066	$80,279,473	$874,258,130

Sources: Arizona Department of Revenue; City of Phoenix; City of Chandler; City of Mesa; City of Tempe; City of Avondale; City of Peoria; City of Scottsdale; City of Glendale; Applied Economics, 2001.

Overall, annual local sales tax collections generate more than $847 million for jurisdictions in Maricopa County. Approximately *90 percent of total local taxes in the county are collected by the six largest cities*: Phoenix, Mesa, Chandler, Tempe, Scottsdale and Glendale. This reflects those communities' large populations and high levels of economic activity. *Of the six industry groups, general retail sales is by far the largest, accounting for an average 52 percent of local sales tax collected.* Retail sales tax collections include most common retail activities such as general merchandise, apparel, furniture, household and garden products, vehicle sales, restaurants and miscellaneous retail.

The distribution of tax collections by industry varies across the jurisdictions and highlights the unique economic structure and the relative dependency on retail sales in each community. *Small and medium size cities and towns that are currently undergoing rapid growth typically show construction activities contributing a large share of the local sales tax.* In the cities of Surprise and El Mirage construction sales tax makes up over 60 percent of their annual sales tax collections, while in other growing jurisdictions such as Fountain Hills, Queen Creek and Buckeye, construction contributes over 35 percent of sales tax revenue. *This finding is key because it indicates the growth stages of each jurisdiction. While these municipalities are currently receiving increased sales tax revenue from construction, construction is also quite cyclical and creates non-recurring revenues. Thus, the amount of sales tax revenue generated may be significantly lower in the long-term if there is not growth in retail or other taxable activities that create a sustainable local tax base.*

On average, tax collections from utilities generate about 11.5 percent of total sales taxes. This share is obviously higher in some cities than others. *Utilities are considered in a separate industry group because they can be taxed at a higher rate, although only a handful of municipalities take advantage of this opportunity. Since utilities are indispensable for residential and non-residential uses, the taxation of gas and electric consumption is a relatively stable source of revenue. In addition, utility taxes can result in significant revenue from industrial and other non-retail developments that tend to be large utility users.* Sales taxes on utility consumption in Chandler and Phoenix make up about 17 percent of collections. This is likely due to the supplemental 1.25 and 0.90 percent tax rates on utilities in each respective city, as well as the substantial levels of industrial development. In comparison, Goodyear, Paradise Valley and Scottsdale have utility tax totaling less than 5 percent of total sales tax collected. Once again, this highlights the diversity of local tax structures and tax-generating activities.

The property category refers to sales tax from rental properties and equipment, such as multi-family residential as well as leases on office, commercial or industrial space and equipment. Municipalities may impose taxes on any, all or none of these activities. Note that only the eight municipalities that collect their own sales tax report rental property categories. This indicates that the other municipalities likely receive sales tax from rental properties but those amounts are listed by the Department of Revenue in other industry categories. *Sales tax on commercial and industrial rental properties is an underutilized resource that could benefit cities with large inventories of leased office and industrial space. Office space in particular with its high lease rates can generate significant revenues.*

Most municipalities have a separate tax imposed on hotel and other lodging facilities. As previously mentioned this tax is charged to short-term lodging providers and sometimes restaurants. All large cities have a transient occupancy tax, while a few smaller jurisdictions do not because they have no hotel establishments. Local transient lodging taxes provide significant revenues for the Town of Paradise Valley, 51 percent, and large shares of sales tax collections in Phoenix, Scottsdale and Tempe. Chapter 5 describes in further detail the impact of tourism on taxable sales in Maricopa County.

Finally, the "other" tax category shows the amount of sales tax collected from generally non-retail and non-residential activities such as manufacturing, mining, real estate, publishing, printing and other industries. These are listed separately because *unlike retail and hotel, activities in this category are not driven by the resident population or the tourism sector, but rather by employment-generating activities.* A comparison of taxes generated from these activities to total employment provides insight into the amount of non-retail economic activity in each jurisdiction (Figure 3-3).

In Figure 3-3, the "Other Tax" category comprises sales tax collected from employment activities described above, plus about 45 percent of the sales tax collected in the property rental category. Sales tax on rental property can indicate employment-driven tax generation from leased office or industrial space. However, rentals also include sales tax collected from residential properties, which are not an employment generating activity. Detailed data from Chandler, Phoenix and Peoria indicate that about 45 percent of the rental property collections come from non-residential activities, therefore for the remaining five cities that report rental property sales, 45 percent of the collections from rentals was added to "Other Tax" collections for comparison.

FIGURE 3-3
NON-RETAIL TAX COLLECTIONS
MARICOPA COUNTY

	Other Tax*	Employment	Other Tax* per Employee
Carefree	$621,770	326	$1,907.27
Guadalupe	$266,031	232	$1,146.68
Cave Creek	$524,473	600	$874.12
Litchfield Park	$951,433	1,125	$845.72
Gila Bend	$93,644	197	$475.35
Surprise	$1,183,143	3,185	$371.47
Paradise Valley	$1,561,226	4,876	$320.19
Goodyear	$2,140,628	7,389	$289.70
El Mirage	$276,694	1,072	$258.11
Fountain Hills	$628,345	2,612	$240.56
Youngtown	$206,464	1,256	$164.38
Buckeye	$326,724	2,576	$126.83
Wickenburg	$135,319	1,071	$126.35
Gilbert	$2,892,721	24,122	$119.92
Queen Creek	$148,449	1,242	$119.52
Scottsdale	$11,907,042	120,874	$98.51
Avondale	$507,570	5,321	$95.39
Chandler	$5,480,707	64,172	$85.41
Tempe	$13,000,532	166,852	$77.92
Phoenix	$56,671,270	784,775	$72.21
Mesa	$7,328,326	150,481	$48.70
Tolleson	$419,732	9,388	$44.71
Glendale	$3,060,775	70,356	$43.50
Peoria	$890,614	20,750	$42.92
Average			$333.14

Sources: Arizona Department of Revenue; City of Phoenix; City of Chandler; City of Mesa; City of Tempe; City of Avondale; City of Peoria; City of Scottsdale; City of Glendale; Applied Economics, 2001.

Surprisingly, there is no direct correlation between per employee tax collections and the size of the community or the development stage, although it appears that small municipalities have the largest per employee rates. There are a few outliers with extremely high per employee rates, which are likely the result of different techniques used in the categorization of sales activity. On average, the other tax category accounts for 13 percent of total sales tax collected. However, in some municipalities where collections are classified by the Department of Revenue, this category accounts for a much higher percent, from 23 to 78 percent. This would lead to higher per employee rates for those jurisdictions.

In the larger jurisdictions, per employee figures are lower. This may be due to a variety of factors including more employment in economic activities that do not generate sales tax such as government or business services. There may be more of these types of jobs in larger cities that have more diverse economies. Also, since each city groups sales tax collections into different categories, it is possible that "Other" tax collections may not incorporate the exact same activities in every jurisdiction.

3.3 Conclusions

The data presented in this chapter indicate important findings about the composition of municipal sales tax collections. *Many growing jurisdictions are presently receiving large amounts of sales tax revenues from construction. While this does not present a problem for larger jurisdictions with diverse economies, it could cause long-term revenue declines in jurisdictions with little other retail or employment-driven activity as construction tapers off and tax revenues generated by construction decline.* Other municipalities have a healthy balance of sales tax generated by retail and non-retail activity, but may need to consider the impact of future growth patterns on long-term local tax collections. The following chapter discusses the national and local retail market trends that may affect the future tax base in Maricopa County.

4.0 *RETAIL MARKET TRENDS*

4.1 Introduction

The purpose of this chapter of the report is to analyze long-term trends in the retail industry, and combine those trends with the information presented in earlier chapters to determine likely impacts on future retail sales potential in Maricopa County communities. These patterns and trends will be key to the financial future of each community, particularly when growth begins to slow significantly thus limiting the expanding pool of new rooftops at the urban periphery to support new retail development. *While even the most remote of these rooftops will have direct revenue impacts through neighborhood-type retail sales in their communities, the ability to capture sales of big-ticket regional and community-type goods will be limited.*

4.1.1 General Role of Demographics and Economics in Retail

The focus of this chapter is on trends in retailing, as they relate to local retail sales and sales tax revenues. However, investigating trends on retailing quickly expands into the study of the key factors driving retail demand, and various alternative providers that satisfy that demand. Thus, trends in retail supply and demand become studies of trends in demographics (market growth, income, age, race and ethnicity), long-term economic growth, retail formats, real estate availability and price, technology advances, etc.

Clearly analyzing the full detail of each of the factors driving the macro retail trends would be beyond the scope of this study. *Rather, the goal of this report is to examine the trends in retailing that are likely to have the most impact on determining the future magnitude and character of retail sales growth within Maricopa County. Focusing on these trends may help communities understand and prepare for some of the opportunities and challenges that lie ahead. Communities will need to consider not only the future size and demographic composition of their resident populations, but also the position of the community in the regional market place and the fast-changing world of retailing.*

4.1.2 Chapter Organization

The balance of this chapter is divided into five sections that frame the importance of retail sales in the region, describe national and local trends impacting retail sales, and then relate those trends to the existing pattern of retail development metropolitan Phoenix area.

Section 4.2 presents a re-cap of information presented earlier in the report on the amount and distribution of retail sales in each community, and provides a brief introduction to retail market potential. The re-cap focuses on the overall importance of taxable sales and retail sales by source for a typology of communities. The introduction to retail market potential describes issues including store versus non-store retailing, the different types and roles of shopping centers, and the concept of trade areas.

Section 4.3 builds on the framework of information on retailing presented in Section 4.2 to examine major trends in the retail industry. This section addresses issues including the long-term decline in in-store retailing, the changing demographic structure of the population, changes in retailing formats, and perhaps most importantly the long-term impact of non-store retailing and the Internet.

In Section 4.4 the industry data and trends and extended through interviews with a select group of real estate and development professionals from the region. The purpose of these interviews is to understand how retailers and developers identify and evaluate sites in Maricopa County, discuss any observations they may have on factors impacting the distribution of retail development within the County, and review the impacts they perceive possible as a result of the trends identified by the background research portion of the study.

The impacts that future trends in retailing identified here may have on retail development in Maricopa County are presented in section 4.5. The section identifies trends that will likely affect the size and distribution of the growth in the retail market as a whole, and then relates those impacts in terms of their implications for communities in Maricopa County. Section 4.6 employs the same basic approach, but focuses on what the trends in retail sales may imply for the revenue structure of local communities.

4.2 Regional & Industry Context

The purpose of this section is to provide background information on the importance of retail sales to communities in the region, and on some fundamental characteristics of the retail industry that will help in understanding the issues.

4.2.1 Sources of Sales Tax Revenue

As shown in Chapter 3.0, there are many sources of the sales tax revenue other than traditional retail sales. Sales tax collection information by community by industry (Figure 3-2, page 14) shows that overall about 50 percent of all local sales tax collections are from traditional in-store retail sales. *When combined with the fact that sales tax revenues comprise 30 to 40 percent of total operating revenues, this implies that 15 to 20 percent of total operating revenues for local communities depend upon retail sales.*

However, it is important to note that data for local communities shows that the share of taxable sales from in-store retailing varies significantly from a low of 2.5 percent Paradise Valley to a high of 69.6 percent in Wickenburg. Among the larger communities Glendale has the highest share of sales tax revenues from retail sales at about 69.5 percent, while Chandler has the lowest at about 45.4 percent. Phoenix, comprising 43 percent of all sales tax collections in Maricopa County, is fairly low at 48.1 percent of sales tax collections from retail.

The balance of sales tax collections is driven by construction, utilities, rentals of real property, hotels and other taxable activity. *Of these, construction currently has the largest overall impact generating about 13.4 percent of all local sales tax collections*. Taxes on utilities are the next largest source of sales tax revenue (11.5 percent), and are fairly consistent across communities. Rentals of real property and hotel/motel rooms, which are only taxed in some communities, make up 7.8 and 5.7 percent of the total, respectively. Finally, other taxable sales including all other commercial and industrial activity comprise about 9.1 percent of the total collections.

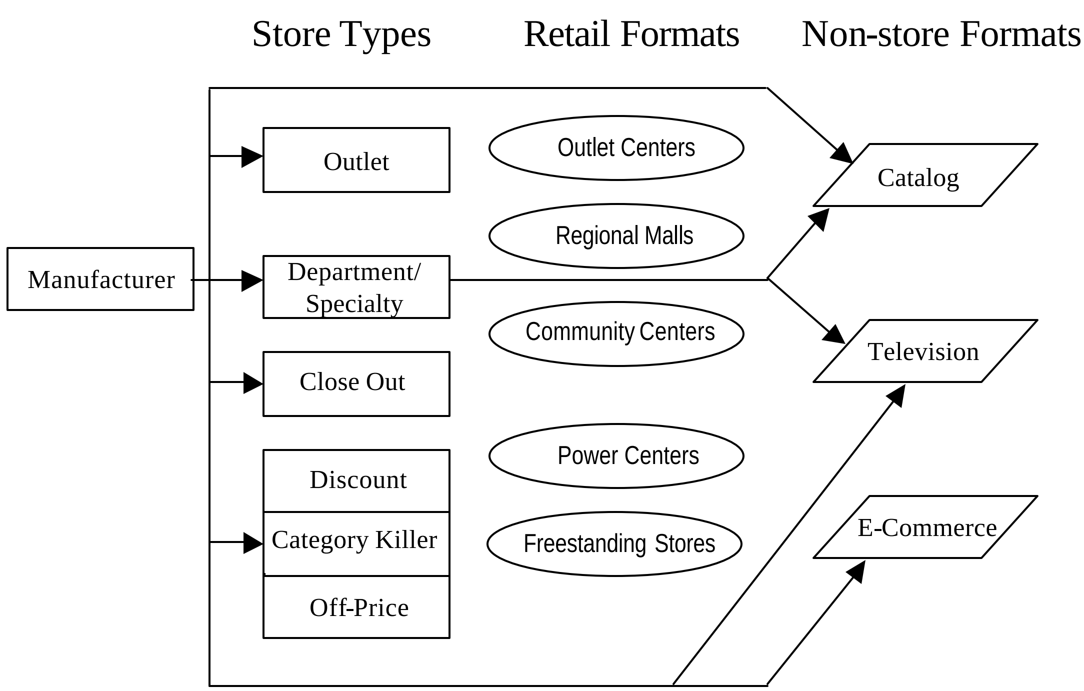
These other sources of sales tax revenue are important to this analysis in that they frame the importance of retail sales, which will become even more important when construction activity declines. Other than construction, these sources represent opportunities for communities to compensate for having a less developed retail marketplace. They also illustrate the importance of tourism-related revenue sources for some area communities including Phoenix, Scottsdale, Tempe and Paradise Valley. Tourism-related expenditures, combined with significant utility and property-rental taxes make Phoenix relatively less dependent upon in-store retail sales than other large communities in Maricopa County.

4.2.2 Retail Sales and Shopping Centers

With in-store retailing generating about 50 percent of local sales tax collections, and with the other sources for generation (other than construction) being relatively more under direct government control, it makes sense to focus study on the future of retail sales in long-term regional planning. The analysis of the regional patterns of retail development, and the retail sales that accompany it, immediately leads to the importance of the various retail "formats," otherwise known as shopping centers.

Figure 4-1 below, developed by Heitman Investment Research, shows how retail demand is satisfied through various store and non-store retailers, and how the store type relates to the various types of shopping centers.[3] According to the International Council of Shopping Centers (ICSC) there are over 44,367 shopping centers in the Unites States, which in 1999 employed over 10.5 million people and collected $47.5 billion in state sales taxes. The vast majority of shopping centers, about 95 percent, are strip centers. Only about 1,800 of the centers are enclosed malls.

FIGURE 4-1
RETAIL DISTRIBUTION CHANNELS



Source: Heitman Investment Research.

While there are some generally held standards for classifying shopping centers, research reveals a number of different typologies that are used. The typologies are generally based on the total size of the center, the number and type of typical anchor tenants and the general marketing concept for the center. The typology shown in Figure 4-2, developed by the ICSC, defines eight distinct types of shopping centers. This typology

[3] White, John R. and Kevin D. Gray, Shopping Centers and Other Retail Properties, John Wiley & Sons, Inc., 1996, p. 116.

seems consistent with the type and concept of shopping centers in Maricopa County, and provides useful information on centers including the tenant mix and primary trade area.

FIGURE 4-2
ICSC SHOPPING CENTER DEFINTIONS -- BASIC CONFIGURATIONS AND TYPES

				Typcial Anchors		Anchor	Primary	Threshold
Type	Concept	Sq. Feet	Acreage	Number	Type	Ratio	Trade Area	Population
Neighborhood	Convenience	30,000 - 150,000	3 - 15	1 or more	Supermarket	30 - 50%	3 miles	50,000 to 70,000
Community	General Merchandise; Convenience	100,000 - 350,000	10 - 40	2 or more	Discount dept. store; super-market; drug; home improvement; large specialty / discount apparel	40 - 60%	3 - 6 miles	100,000 for Discount dept.; 75,000 for Wholesale Clubs
Regional	General Merchandise; Fashion (Mall, typcially enclosed)	400,000 - 800,000	40 - 100	2 or more	Full-line dept. store; jr. dept store; mass merchant; disc. dept. store; fashion apparel	50 - 70%	5 - 15 miles	250,000+ in metro area
Superregional	Similar to Regional Center but has more variety and assortment	800,000 +	60 - 120	3 or more	Full-line dept. store; jr. dept store; mass merchant; fashion apparel	50 - 70%	5 - 25 miles	400,000+
Fashion/Specialty	Higher end; fashion oriented	80,000 - 250,000	5 - 25	N/A	Fashion	N/A	5 - 15 miles	100,000 small; 450,000+ large
Power	Category-dominant anchors; few small tenants	250,000 - 600,000	25 - 80	3 or more	Category killer; home improvement; disc. dept. store; warehouse club; off-price	75 - 90%	5 - 10 miles	150,000 for home impr.; 75,000 to 100,000 for other store types
Theme/Festival	Leisure; tourist-oriented; retail and services	80,000 - 250,000	5 - 20	N/A	Restaurants; Entertainment	N/A	N/A	na
Outlet	Manufacturers' outlet stores	50,000 - 400,000	10 - 50	N/A	Manufacturers' outlet stores	N/A	25 - 75 miles	na

Source: International Council of Shopping Centers, June 2000; Urban Land Institute, "Shopping Centers and Other Retail Properties," 1997.

Each type of shopping center draws a different group of retailers with each group seeking to target a particular geographic area and market basket of goods. For example, neighborhood centers offer convenience goods, including a supermarket, ranging from 30,000 to 150,000 square feet on 3 to 15 acres serving a primary trade area of 3 miles. Community centers, which range from 100,000 to 350,000 square feet offer a true mix of convenience and general merchandise goods, and include anchors such as discount department stores, home improvement stores, large specialty/discount apparel and supermarkets.
Community centers typically serve market areas of 3 to 6 miles in radius.

Regional and super-regional centers offer a general merchandise, apparel and furniture, and are typically anchored by 2 or more full line department stores. Regional centers range in size from about 400,000 to 800,000 square feet and serve primary trade areas of 5 to 15 miles. Super-regional centers are 800,000 square feet or more, and can draw from as far away as 25 miles.

The balance of the types of shopping centers includes a number of formats that address particular retail concepts such as fashion/specialty centers, power centers, theme centers and outlet malls. For the most part these retail formats serve large primary trade areas of 5 to 15 miles in radius, with outlet centers drawing customers from up to 75 miles away. Fashion centers, located only in affluent areas, offer higher end, fashion oriented merchandise. Power centers specialize in category killers including home improvement centers, discount department stores and warehouse clubs. Theme centers, which can include restaurants and various forms of entertainment, are unique among the types of centers in that the primary trade area is not limited by geography. These are generally one-of-a-kind attractions that may be more influenced by non-resident than resident populations. Finally, outlet centers provide manufacturers the opportunity to market direct to the public, and offer a broad range of apparel and other general merchandise to consumers in a very large market area.

One observation that can be made about the types of shopping centers as they relate to local retail sales is that other than convenience goods, it may be very difficult for a community to capture general merchandise purchases by it residents. This would imply that communities near the urban periphery would have difficultly generating significant retail sales due to the relatively large trade areas of existing community and regional shopping centers. As the urbanized portion of the county expands, new areas attain critical levels of demand for these goods, and new community and retail center are constructed. This would imply however that communities developing later, and those at the extreme edge of the urban area, could never generate the same level of retail sales as established, more centrally local communities.

4.2.3 Existing Retail Trade Patterns

The varying nature of the communities in the retail marketplace of Maricopa County, combine with forces driving retailers and the shopping centers they occupy to dictate the type and level of retail sales in each community. While the manifestation of these forces is different in every community, there does begin to emerge a grouping of communities that may be useful in identifying the future trends in retail sales potential. This grouping system includes:

- **The Establishment** – Existing retail hubs/tourism meccas
    - Phoenix, Mesa, Scottsdale and Tempe
- **Rooftops & Revenues** – New suburban communities
    - Avondale, Chandler, Glendale, Goodyear and Peoria
- **Late Arrivals** – Emerging edge communities
    - Gilbert, Queen Creek and Surprise
- **Residential Retreats** – Retail not important part of land use
    - Paradise Valley, Fountain Hills, Litchfield Park and Youngtown
- **Out on the Ranch** – Better capture of local expenditures due to distance
    - Carefree, Cave Creek, Gila Bend and Wickenburg
- **Retail Challenged** – Communities with challenges
    - Buckeye, El Mirage, Guadalupe and Tolleson

Whatever may lie ahead in terms of retail trends, the impacts on the communities in each of these groups will be very different. For *The Establishment*, there will be the long-term need to remain competitive with alternatives provided in the new and emerging suburban areas, however there is little chance of losing great market capture. Each of these communities is a recognized center for business, trade and commerce, and will only be significantly impacted by external trends in retailing, some of which are discussed in section 4.3.

For the *Rooftops & Revenues* group the future is very bright, again with external trends withstanding. These communities have achieved a level of saturation in their local retail markets that is commensurate with their size, and either by physical location or other attributes are succeeding in generating sales tax revenue. The *Late Arrivals* group may someday have the level of retail sales exhibited by the Rooftops & Revenues group, however the total potential may be limited by timing and location. These communities are the most at risk from not only competition, but from future trends in retailing.

Residential Retreats consist of communities that have, by choice, a very low level of retail development, and thus will not likely be affected by any trends in retail sales. The next group, Out on the Ranch, includes a group of communities that are somewhat similar to the Residential Retreats, except with a higher level of retail sales due to their relatively isolated locations and significant tourism impacts.

The final group, *Retail Challenged*, includes communities that do not have significant concentrations of retail development, and thus lag in retail sales. Like the Late Arrivals group, these communities are in danger of never generating retail sales commensurate with their population, due to both competition and trends in retailing.

4.3 Macro Industry Trends

This section of the analysis focuses on macro trends in the retail industry that will have an effect on the amount and distribution of future retail sales and development in Maricopa County communities. These trends range from changing preferences of consumers, to the changing profile of the American shopper, to new retail formats, to the impact of technology and e-commerce.

4.3.1 Declining Growth of Retail Sales

One of the most important macro trends affecting retailing in the future is overall decline in the growth rate of retail sales. Based on data from *Monthly Retail Trade*, a publication of the U.S. Bureau of the Census, the Urban Land Institute (ULI) has calculated that the average annual inflation-adjusted growth in retail sales has fallen from 2.6 percent in the 1980 to 1985 period, to 2.5 percent in the 1985 to 1990 period, and to 2.1 percent in the 1990 to 1995 period. Adjusting these growth levels for the change in population in the U.S. results in a long-term net stagnation or slight decline in per capita retail sales.

The ULI book, *The Retailing Revolution* attributes this decline to the aging of the baby-boom population, and decreases in consumers' purchasing power due to stagnating household incomes and escalating debt burden. Spending for discretionary purchases has fallen as a share of total spending. *In general, shopping centers survive on discretionary spending, and thus are losing ground in the competition for consumer dollars.*

Declines in the real level of retail sales, combined with continuing construction of new retail space at the rate of about 44 million square feet per year, have resulted in *a dramatic rise in the per capita amount of retail floor space.* Overall, there was a 68.9 percent increase in the GLA per capita in the U.S. between 1970 and 1990.[4] This continuous addition of new space also forces existing shopping centers to constantly renovate and re-target themselves to compete.

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[4] Shopping Centers and Other Retail Properties, p. 116.

This trend has gone almost unnoticed in Maricopa County due to rapid population growth, creating the illusion of ever-expanding retail market potential. When/if growth begins to slow significantly in the future this trend may impact all communities. This is certainly going to be an issue for each municipality as the last stage of development – approaching build-out – is approached.

4.3.2 Impact of Non-Store Retailing

In 1996, non-store retailing captured only about 3 percent of the activity in the $2.48 trillion U.S. retail industry, or about $71 billion.[5] When retail sales are adjusted to exclude automotive sales, the non-store total still represents only about 4 percent of total retail trade. However, when total non-automotive retail purchases are adjusted to account for sales at shopping centers only, the total falls to $934 billion, making non-store retailing equal to about 7.6 percent of shopping center retail sales. *This rapid market penetration is important since most non-store retailers typically compete for sales of general merchandise, apparel and furniture (GAF) – the same market basket of goods that drives community, regional and power/fashion/specialty shopping centers.*

Historically catalogs companies such as Spiegel and Land's End, and mass merchandisers such as Sears and J.C. Penney have dominated non-store retail sales. Catalog merchandisers have enjoyed annual sales growth rates of 5 to 7 percent in recent years, far out-stripping the 2.5 percent annual growth in overall retail sales. Beginning in the late 1980's, television began to be used widely for direct marketing with networks like Home Shopping Network and QVC. Television retail sales grew from a $920 million per year business in 1988, to more than $2.7 billion in 1996, according to data from the WEFA group compiled from the television sales networks.

The most recent, and by far the most important trend in non-store retailing is e-commerce. At about $500 million in 1996, retail sales on the Internet were a totally insignificant component of retail trade. Current (1999) data for online retail sales shows a 40-fold increase between 1996 and 1999 to about $20 billion per year – which is still only about 2.2 percent of shopping center sales of over $900 billion per year. However, the non-store share of GAF is rising considerably faster than is the non-store share of total retail sales. Thus catalog sales and Internet sales cut into shopping center sales disproportionately.

Most industry experts predict that the Internet and e-commerce will continue to grow rapidly, having a significant impact on the retail marketplace and capturing a significant share of GAF purchases – directly impacting shopping centers and thus local retail sales. Some predictions show the share of non-store GAF sales more than tripling over the next 10 years from about 15 percent to 55 percent.[6] Other predictions are less aggressive, but all expect substantial growth in non-store retail sales, particularly e-commerce. Another way to put the potential impact of e-commerce into perspective is reported in the ULI book, *Cities in the 21st Century.* The book quotes the Center for Energy and Climate Solutions estimate that *by 2007 e-commerce may prevent the need for 1.5 billion square feet of retail space and 1 billion square feet of warehouse space nationally.*[7]

However, a great deal of uncertainty still exists in predicting the extent of the impact. Five nationally known e-commerce consulting companies prepared e-commerce sales projections for 2003 ranging from $75 billion to about $144 billion. [8] [9] If total e-commerce were to reach $144 billion, it would likely capture between 10 and

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[5] Schwartz, Mary B., The Retailing Revolution, Urban Land Institute, 1997, p. 17.
[6] The Retailing Revolution, p. 26.
[7] Urban Land Institute, Cities in the 21st Century, 2000, p. 28.
[8] International Council of Shopping Centers, "E-Commerce," Spring 2000, www.icsc.org/rsrch/wp/ecommerce.

15 percent of current shopping center sales affecting both established and evolving retail markets in Maricopa County.

4.3.3 Retail Sprawl

Consistent with pattern of neighborhood and community shopping centers following new rooftops in Maricopa County, there has been a national resurgence in the performance of neighborhood centers. A May 2000 article titled *Suburban Shopping Center Numbers Show Consumer Support for Sprawl*, reports on a ULI study linking suburban sprawl to the recent success of neighborhood shopping centers. According to the study, *neighborhood shopping centers are the top performers among the four major shopping center types,* with average tenant sales of $260.49 per square foot. Sales per square foot at neighborhood centers were up 21 for the three years ending in 1999.[10]

This trend may bring great joy to the Rooftops & Revenues, Late Arrivals and the Out on the Ranch groups of community retail markets in Maricopa County. The enhanced ability of neighborhood and community specialty centers to meet consumer demand at the local level should lead to greater tax revenues in the future. This could help offset the fact that many of these communities will never be in a position to support a regional or super-regional shopping center due to the expanse of existing primary trade areas. In fact, the offset could be enough to have a negative impact on some of the existing regional retail centers in established areas.

The same study reports that *older, smaller and often poorly located regional shopping centers are being "out-flanked" by community power centers offering lower prices*. The trend has not extended to super-regional shopping centers however, with those centers continuing to out-perform all the other major center types in terms of net operating balance at $20.67 per square foot.

4.3.4 Decline of Department Stores

According to an April 2001 article in *Shopping Center World*, the *future of traditional department stores, the cornerstone of many super-regional centers, is in question*. "Many department stores are doomed," says R. Fulton MacDonald, president and CEO of International Business Development Inc., a consulting firm specializing in retail. He says, "I don't mean every department store will go completely out of business. But the ones that remain will have to re-invent themselves."

A study by PriceWaterhouseCoopers suggests that the woes of the department store industry stem from too many department store names competing for a dwindling pool of dollars. According to this study, conventional department stores (not including mass merchandisers such as Sears and J.C. Penney), accounted for 3.5 percent of non-auto retail sales in 1990, and just 2.3 percent in 2000. It is anticipated that the share could fall as low as 1.9 percent by 2005.[11] *This trend may force super-regional mall owners and the communities that host them to evaluate options for the re-use of some of this space. This trend would again be more of a threat to communities with well-developed retail bases.*

4.3.5 New Retail Formats and Standards

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[9] Cisco Systems, "Net Index," 2000, www.cisco.com/warp/…en_tre_net_0023/gen_tre_net_0023_l.shtml.
[10] Hensell, Lesley, "Suburban Shopping Center Numbers Show Consumer Support for Sprawl," Realty Times, May 25, 2000, www.realtytimes.com/rtnews/rtcpages/20000525_shoppingcenter.htm.
[11] Fickes, Michael, "Doom to Boom?" *Shopping Center World*, April 1, 2001.

Another macro trend in the retail industry that could affect the distribution of retail sales in Maricopa County is *the advent of several new retail formats* (types of shopping centers), and changing service delivery techniques and standards in traditional shopping centers. New retail formats continue to emerge based on totally new concepts and various combinations of old ones.

The most dominant of the newer retail formats are power center and value malls. While not a new phenomenon, these types of centers will continue to have an impact on community and regional retail shopping centers, especially in newly developing areas of the County. The effect is much the same as that of "retail sprawl" described above, except that these centers cut even further into the GAF sales that support larger, traditional regional and super-regional shopping centers.

The impact of power centers and value malls was already having an impact in the early 1990's. At that time it was reported that traditional shopping centers with 30 to 40 percent anchor tenant space would continue to be adversely impacted by the newer power center configurations that contain as much as 60 to 70 percent anchor space, much of which may be occupied by 'category killers' or warehouse club retailers.[12] Large power centers may contain up to 10 "power anchors," including the aforementioned category killers and discount department stores, super drugstores, supermarkets and off-price apparel stores. According to *brainreserve.com*, discount/off-price outlets are the fastest growing sector of retail, with one-third of all groceries now being bought at warehouse clubs.[13]

In a related trend that could have definite implications for future retail development, builders in Maricopa County are changing the shape of many strip centers to accommodate a mix of power anchors. While accommodating the power anchors often requires substantial expansion or re-configuration, community centers in the right market situation are being re-designed and re-positioned to meet this trend. Locally, Thomas Mall (now Arcadia Crossing) and Tower Plaza are but two examples of this concept.

In addition to new retail formats, there are other trends in the retail industry that may have an impact on the amount and distribution future retail development in Maricopa County. These trends include:

Increasing traditional anchor sizes. The increasing *space requirements of typical neighborhood and community center anchors require larger sites*. The larger stores of course also require a larger market base, reducing the number of centers built.

More culture, entertainment & services (regional centers). In order *for regional, super-regional and theme centers to be successful they will need to offer a broader range of services, resembling that of a town center.* In addition to retail stores, centers will need new amusement features such as cinemas and food courts, and other services such as dry-cleaners, hair salons, video/DVD rental stores, etc. There will also be a need for brick-and-mortar retailers to distinguish themselves by focusing on the better quality in-store service.

High-quality design. Hand in hand with high-quality service is the need for high quality space. *The challenge here falls more on shopping centers in established areas that are forced to continually re-make, and in some cases re-target themselves to compete with new centers and concepts*. Data from the ICSC's *Handbook on Shopping Center Operation* reports that the average time since last alteration of a center was 3.9 years. The same study found that only 17.5 percent of all malls have never been expanded or re-modeled.[14] In general, the larger the center, the more likely it was to have been renovated.

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[12] Schwanke, Dean, Remaking the Shopping Center, Urban Land Institute, 1994, p. 9.
[13] Popcorn, Faith, "Vigilante Consumer," www.brainreserve.com/trends/vigilante.htm, accessed 4/30/01.
[14] Remaking the Shopping Center, p. 11.

Institutional Ownership. The shift to more institutional ownership of shopping centers, and REITs (Real Estate Investment Trusts), has contributed to more aggressive management of properties. These owners often employ a strategy of acquiring under-achieving centers, and then making the necessary capital investment to manage the asset for the long term. *This trend will like result in a more bottom-line approach to retail center survival, with successful centers being vigorously managed and promoted, and unsuccessful centers being closed.*

4.3.6 Shifting Demographics

A final, but by no means insignificant trend impacting the retail industry and retail sales is the changing demographic characteristics of the population. *On a national and regional level this has resulted in a number of specialty products and stores serving specific high-growth demographic groups. These groups include the elderly, minority and ethnic groups (especially Hispanics in the case of Maricopa County), single parents, etc.* The generally lower income levels associated with these groups will have implications in terms the market basket of goods consumed, and the amount of money remaining for the types of discretionary purchases that drive community and regional retail sales.

At the local (center by center) level, the implications of shifting demographics can be far more important. According the ULI's *Remaking the Shopping Center*, each shopping center has its own market area characteristics that change gradually, or rapidly over time. *The demographics and character of a market can change dramatically in 10 to 15 years in terms of average age, income and other characteristics. This change often requires repositioning of a center, especially its tenant mix, to better take advantage of the surrounding market.* Center owners should prepare a new demographic profile of the market area at least every ten years, with additional tuning after five years, in accordance with new Census information. It is equally important to evaluate the geographic draw of the center to validate the size of the primary trade area.

The primary demographic factors considered by retailers in evaluating a market area include the number of households in the primary trade area, and the income and age characteristics of the occupants.[15] Other demographic factors like education, occupation and ethnicity are less commonly used in analyzing local retail markets. Education is considered to be closely correlated with income, but can be important to some retailers such as booksellers, while occupation is only important to retailers such as office supply, music and video stores. Ethnicity is seldom designated as a site criterion, but it is critical in the subsequent merchandising and operation of a retail business or shopping center.

With the projected aging and expanded demographic diversity of the population of Maricopa County, communities and retailers will need to pay particular attention to the needs of area residents. Being in tune with these factors can help nearly every community maintain a successful base of neighborhood and community shopping centers.

4.3.7 Other Forces Affecting Retail Trade

Beyond the retail industry itself, there are major trends predicted for metropolitan areas that could also have an impact on future retail sales. Some of these trends are also discussed in earlier sections, while others

15 Shopping Centers and Other Retail Properties, p. 130.

represent unique but often related trends. According the ULI book *Cities in the 21st Century*, the ten most likely influences on the American metropolis for the next 50 years will be:

1) Growing disparities of wealth
2) A suburban political majority
3) The aging of the baby boomers
4) A perpetual "underclass" in central cities and inner-ring suburbs
5) "Smart Growth": environmental and planning initiatives to limit sprawl
6) The Internet
7) The deterioration of the "first-ring" post-1945 suburbs
8) Shrinking household size
9) An expanded superhighway system of "outer beltways" to serve new "edge" cities
10) Racial integration as part of the increasing diversity in cities and suburbs.

4.4 Metro Phoenix Industry Insights

This section highlights information obtained from local real estate professionals to validate the findings from the background research. The section is organized around the primary observations expressed by those interviewed. These observations include general trends in the size, location and market area for particular types of centers; the prognosis for outlying/edge communities; and observed long-term trends in retailing.

4.4.1 Type, Size and Separation of Centers

Many of the trends described in the literature regarding the type and size of shopping centers now being constructed were verified through discussions with local industry experts.

One of the trends confirmed was that of *larger anchor tenants, and a wider variety of services and neighborhood shopping centers*. According to Alan Zell, Zell Commercial Real Estate Services, the overall size of neighborhood centers has not increased dramatically, but the *space required by supermarkets has grown* from 30,000 to 40,000 square feet to 50,000 to 60,000 square feet. Gone from the centers are many other larger tenants like hardware stores and auto parts stores.[16] *Now, the remaining space tends to be subdivided among an increased number of smaller users, resulting in a wider variety of services being offered at neighborhood shopping centers.* These services tend to include restaurants, food preparation and delivery services, insurance agents, tax preparation services, video rental stores and other personal services. Some of these retailers are also looking for ways to reduce their need for space through the use of technology, and by limiting the range of alternatives provided. Mr. Zell noted that Blockbuster Video recently reduced its store size from 6,000 square feet to 4,000 square feet by focusing on first-run movies, instead of offering the full range of "classic" files. He added that neighborhood centers in the urban part of Maricopa County anchored by supermarkets tend to have primary trade areas of 2 to 3 miles in radius.

Bob Kammrath, of Kammrath & Associates agreed, adding that the larger format of stores, especially in community shopping centers, makes them even more sensitive to changes in primary trade area and the local economy.[17] This trend, combined with that fact that larger stores tend to be under corporate ownership/operation, means that *centers and communities face increased problems from "instant" store closings*. Gone are the times when even large retailers were able to carry non-performing stores for any significant period of time.

[16] Phone interview with Alan Zell, Zell Commercial Real Estate Services, June 21, 2001.
[17] Phone interview with Bob Kammrath, Kammrath & Associates, June 21, 2001.

Interestingly, both Mr. Kammrath and Mr. Zell identified *community power centers as a threat, one to regional retail and the other to neighborhood retail*. The growth in this retail format has clearly already had a dramatic impact on retailing in Maricopa County. This trend may accelerate in Rooftops & Revenues and Late Arrivals communities, as the new format will become a bigger part of the retail marketplace from the beginning.

4.4.2 Trends for Outlying/Late-Arrival Communities

Mr. Zell confirmed that larger or more diverse neighborhood centers could capture an increased level of sales in communities that lack nearby competition from power centers and regional malls. He suggested that such communities make an effort to attract retailers selling a wide variety of products. *The goal would be to manage retail development at the community level to ensure that a full range of goods is available to consumers locally.* This is consistent with observations made in the research, and can lead to a practice called centralized retail management that is discussed in Section 4.5.4.

In order to make it more possible to achieve the goal of capturing sales from residents and others, *small and growing communities must take care not to discourage retail development with their planning policies and other government restrictions*. According to Mr. Zell, communities must make an effort to provide convenient access, ample parking and increased visibility to make local retailers a success. This effort also includes such items as sign ordinances and landscaping requirements that effectively "hide" the businesses from consumers.

4.4.3 Other Observed Retail Trends

Some of the most interesting information on long-term retail trends was provided by Bob Kammrath, of Kammrath & Associates in Phoenix. The observations made by Mr. Kammrath validate *the threat posed to regional malls by large community power centers*. According to Kammrath & Associates the past few years have seen the removal of six enclosed malls from the local inventory. While a few of the sites have/will re-emerge as shopping centers, a number have disappeared for good. Mr. Kammrath sites the weak position of many department store tenants as major factor contributing to the demise of regional centers. "The impact of these events varies from location to location. At some properties the empty space will probably soon be filled by a replacement store of a similar type. At others, the departure of one more old-line retailer could mean a complete make-over of the center or worse." He also notes that *the share of retail space in Maricopa County represented by regional malls has decline steadily over the past 10 years*.

4.5 Retail Development Implications

Based on the information presented in the previous sections, this section draws conclusions about how the various trends in retailing will impact retail development, and hence retail sales in Maricopa County and its communities. These implications include, but are certainly not limited to the following.

Fewer Centers and Less Overall Space. The declining rate of growth of in-store retail sales, the increasing growth of e-commerce, changing demographics, stagnating household incomes and larger store sizes imply there will be less new space developed, some (less-competitive) existing space will need to be re-used/re-developed, and the total number of centers will likely decline when population growth begins to slow.

Reduced Development Potential for Edge/Late-Expanding Communities. Closely linked to the decline in sales potential, is the reduced community, regional and super-regional sales potential of later developing communities. Due to the size and quality of the established retail base in Maricopa County, and the significant trade physic al trade area that these centers require, it is unlikely that edge and later developing communities will ever capture their "fair share" of retail development and sales. This results in a permanent inequality being formed between the communities of Maricopa County with respect to local sales tax generation.

More/Bigger Neighborhood Centers – Retail Sprawl. One likely impact of future trends in retailing that will help to offset the lack of community and regional retail development in edge/late-expanding communities is the expanded role of neighborhood and small community centers. In the spirit of making things as convenient for the consumer as possible, the recent trend in expanding the role of the neighborhood center to include more goods and services will mean more or larger centers in newly developing areas. This impact may also be felt in more established areas, although typical site size requirements limit the implementation in developed areas.

This trend will result in more focus in developing communities on bigger, more diverse anchor tenants in neighborhood centers, a continued scramble to attract Big Box/Power Center developments, and more focus on specialty stores and entertainment destinations.

More Redevelopment and Revitalization of Prime Areas. The increased competition created by shrinking retail store markets, and the addition of new, better neighborhood and community retail centers in the urban periphery will put even more pressure on redevelopment and revitalization efforts. Attracting retailers, shoppers and other users to older, often less affluent areas will become an even bigger challenge than it is today. However, it is a challenge that needs to be addressed, especially as urban areas become more densely developed in the future. One of the possible scenarios for the future in *Cities in the 21st Century* involves a fundamental shift in the basic framework of building and development back to the urban core.

One concept discussed to help with revitalization efforts is centralized retail management (CRM). CRM goes beyond the traditional promotional or physical improvements that have too frequently produced disappointing long-term results. According to Jack R. Stokvis, Assistant Secretary of the U.S. Department of Housing and Urban Development, "CRM builds on many long-established methods of revitalizing downtown retailing, and adds to them the newer ideas of control over retail mix and cooperation among property owners. It seeks to create organizational and financial arrangements to embody this cooperation. In short, it tries to replicate the successful common control elements that are, in large part, the reasons for the success of modern shopping centers."[18]

Applying this principle to the downtown setting, with many owners and interest groups can be very challenging. Yet an increasing number of communities have recognized the advantages of implementing CRM. CRM has been refined and applied to a variety of downtown settings over the past several years. The CRM strategy encompasses four distinct elements[19]:

1) **Market Emphasis**. Understanding the role that the area can play in the local economy and capitalizing on it.
2) **Enlistment of All Interested Parties**. CRM must bring together landowners and retailers with municipal planning and economic development officials, traffic engineers, financial institutions, major employers and hotel managers.
3) **Coordination of Both Leasing and Retail Practices**. As the most distinctive of the features of CPM, this may also be one of the hardest to achieve. Coordination of leasing may require pooling of owners' retail properties or spaces in exchange for share in a common enterprise, or it may be accomplished through informal agreements.

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[18] Stokvis, Jack R., Making Downtown Competitive Again, Urban Land Institute, April 1987, p. 8.
[19] Cloar, James A., Centralized Retail Management, New Strategies for Downtown, Urban Land Institute, 1990, p. 5.

4) **Management and Enhancement of the Total Retail Environment**. CRM embraces downtown management practices that are already well accepted and in place. It ensures that these practices further rather than undercut retail objectives by influencing parking, retail frontage continuity, streetscape improvements, building facades, and other factors that shape the shopping experience.

An implication of these trends for communities in Maricopa County is to re-focus more of their long-term retailing strategies on downtowns and other dense urban nodes. And, even though downtowns are the most likely place for many cities to focus, a larger overriding implication is the need to focus energy on a few, most competitive areas that the established part of the community has to offer.

More Redevelopment of Older Regional Centers. Due to shrinking retail store markets, retail sprawl and changing retail formats there will likely be more remodeling of older regional and super-regional centers, along with the closing of centers with poor locations or demographics. Older centers will need to be periodically remodeled, and their market areas will need to be reevaluated to stay in tune with the needs of the market area population. This means that regional retail center managers will need to adjust the tenant mix over time to respond to these changes. Smaller regional centers will likely be more at risk, as they have neither the market potential nor the development potential (site size) to compete with new centers.

4.6 Local Revenue Implications

The implications of the trends in the retail industry, and the trends in non-store retailing, may have a dramatic impact on the way communities view retail sales, and sales taxes. The purpose of this final section is to translate specific trends into likely positive and negative revenue impacts on groups of communities in Maricopa County. The typology of cities presented in section 4.2.4 is used to group communities for this portion of the analysis.

4.6.1 Declining Overall Retail Sales Taxes

Changing demographics, increasing consumer debt burdens, and stagnated household income growth are all contributing to lower levels of per capita retail sales. This trend may result in a long-term decline in retail sales generation across all groups of communities. There will continue to be winners and losers among communities relative to retail sales, but adjusting for population growth, most communities will experience a real decline in retail sales and retail sales taxes, in the long-term.

4.6.2 Loss of Local Sales Tax Revenue to Non-Store Retailing

The evolution of non-store retailing may have a significant impact on local sales tax generation, especially when taken in tandem with overall declining levels of retail sales. Since non-store sales generally have a disproportionate impact on GAF, this trend could cause a greater impact in communities that are heavily dependent upon large community and regional shopping centers for sales tax revenue. This trend would seem to be the greatest threat to communities in The Establishment and Rooftops & Revenues groups, although the trend may have both long-term development and revenue impacts in the Late Arrivals group of communities.

4.6.3 Increased Revenues from the Information Economy

The potential losses in sales tax revenues that are possible due to the impact of non-store retailing, and specifically e-commerce, have not gone unnoticed by state and local government officials. In Arizona, the state has established the Joint Legislative Study Committee on Internet Issues. The goal of the committee is to explore ways for Arizona to take advantage on the Internet's potential, as well as forming defenses against "cyber threats." A key principal developed by the committee states:

> "Providing special treatment to one sector of the economy, to the disadvantage of other competing sectors, does not make rational economic or tax policy. Government should provide uniform treatment for all. Requiring that sales and use taxes be collected on all like transactions is an equitable tax policy approach." [20]

While there are many details of this approach to be resolved, it seems reasonable to assume that in the long term some of the losses in local retail sales taxes due to non-store purchases will be compensated through some form of revenue sharing. It is likely that the state would assume the lead role in this program, establishing methods of tracking retail sales by Arizona residents on the Internet, and collecting and distributing those revenues based on a revenue sharing formula.

4.6.4 Moving Revenues Through Retail Sprawl

The potential impacts of retail sprawl may be one of the best reasons to promote regional sales tax revenue sharing. This trend generally results in newer, larger, more sophisticated neighborhood and community centers being built in close proximity to new rooftops – wherever they may be. This trend has been fueled in recent years by the success of big box and power center types of retail development. The sales tax revenue impacts of this trend will certainly be negative on communities in The Establishment group, and in the longer term the Rooftops & Revenues group. However, it could have a very positive impact on the Late Arrivals, Out on the Ranch, and perhaps even the Retail Challenged groups of communities.

4.6.5 Declines in Construction-Driven Sales Tax Revenues

While not driven by trends in the retail industry, it is important to note that as the aforementioned trends are coming into full fruition, construction activity in Maricopa County will slow during recessionary periods. This could result in local governments, especially communities in the Rooftops & Revenues and Late Arrivals groups, to be hit with declining sales tax revenues on two fronts simultaneously.

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[20] Arizona Legislature Internet Study Committee, "Positioning Arizona to Achieve Maximum Benefit from the Information Economy," 2000, Final Report p. 3.

4.6.6 Increases in Other Local Funding Sources

The bottom line with respect to local sales tax revenue, is that it will likely decline in real, growth-adjusted terms over time, and communities will need to tap other local funding sources to make up the difference. Leveraging more heavily on purchases people make in neighborhood centers including food and drugs could make up some of the difference. However, it is more likely that other local revenue sources may need to be employed to a greater extent including local property taxes, utility taxes and user fees. This impact will likely be experience by all jurisdictions, except those that are not dependent upon retail sales tax including the communities in the Residential Retreats and Retail Challenged groups.

5.0 *TOURISM TRENDS*

Tourism is a key component of Arizona's economic base, as well as its sales tax base. This section will quantify the current level of tourism and related expenditures in Arizona and Maricopa County, as well as present information on national and local trends in tourism. Similar to retail centers, the demands of consumers change as lifestyles and demographics change and local hospitality providers must keep up with these new demands in order to maintain market share in a competitive environment.

5.1 Current Tourist Expenditures

Tourism nationally is a much larger sector than many people realize. Expenditures by domestic and foreign tourists contribute more than $502 billion to the national economy each year. Based on the types of expenditures, this makes tourism the third largest retail segment with over $71 billion in tax revenues to federal, state and local governments annually.[21]

Arizona has approximately 25 million tourists visit the state each year.[22] There are four industries that are primarily impacted by these tourist expenditures: lodging, restaurants and bars, retail and entertainment and recreation. Tourists spent more than $6.4 billion in these sectors.

According to the United States Travel Data Center, Arizona ranks 4h among western states in terms of total domestic and international tourist expenditures with total expenditures estimated at $7.2 billion. Nine of the thirteen western states, including Arizona are among the top thirteen states in the nation in terms of total tourism employment. [23]

Maricopa County has more than 11 million visitors each year and annual expenditures of about $5 billion. The largest portion, 30 percent, is spent on transportation including airfare as well as local transportation. This amounts to about $1.42 billion in transportation expenditures. Sky Harbor Airport estimates a direct economic impact of $8.4 million and a total economic impact of over $16 million to firms directly involved in passenger and air cargo movement including airlines, airport businesses, fixed base operators, air cargo providers and ground transportation.[24]

The region's more than 45,000 hotel rooms attract an estimated $948 million in expenditures, and capture about 20 percent of tourism dollars. Food and beverage sales account for an additional 20 percent of expenditures. Other major categories include retail sales at $664 million (14 percent), entertainment at $527 million (11 percent) and other expenditures of $231 million (5 percent).25 State sales tax collections on lodging, food & beverages, entertainment and retail sales amount to at least $154 million per year from tourists. This is about 5 percent of the total amount of sales tax collected by the state. Local sales taxes vary depending on the city, but based on average tax rates these tourism expenditures generate about $77.4 million in sales and lodging taxes to cities in Maricopa County. This is about 13 percent of the total amount of regular or general fund sales tax collected by cities, and about 9 percent of total city sales tax collections in Maricopa County. While local residents and businesses generate the majority of sales tax collections, tourism is certainly a key component.

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[21] Arizona Tourism Alliance, "Tourism Industry Facts." 1999.
[22] Greater Phoenix Convention and Visitors Bureau, "1999/2000 Statistical Summary." 2000.
[23] Western States Tourism Policy Council, "Economic Impact of Tourism in the West." 1999.
[24] Phoenix Sky Harbor International Airport, Economic Impact, 1998.
[25] Greater Phoenix Convention and Visitors Bureau, 2000.

A separate category of visitors is motor home and travel trailer winter visitors. They typically stay about four months, and while they do not spend money on hotels, they inject a large amount of money into the local economy through other types of purchases. In total, the approximately 120,000 winter visitors to Greater Phoenix each year account for about $370 million in direct expenditures locally.[26]

Conventions are also a particularly important segment of the tourism economy. The Phoenix Civic Plaza alone generates about 185,000 room nights per year from out-of-town attendees. The revenue from these room nights was estimated at $82 million for 2000.[27]

5.2 Local Distribution of Tourism

Lodging inventory is a good indicator of the local distribution of tourism expenditures. In 1999, there were an estimated 45,700 hotel rooms in Maricopa County. The largest share, 51 percent, was in Phoenix including the East, West and Airport sub-markets. The next largest portion, 26 percent, was in Scottsdale. Other major sub-markets include Tempe (11 percent) and Mesa/Chandler (12 percent). About 37 percent of the total rooms were considered luxury or upscale, 37 percent were budget or economy, and 26 percent were mid-priced rooms.[28] Since room taxes are based on room rates, the luxury and upscale rooms generate the most tax revenues.

In the past two years, the area has added a large number of mid-priced and economy rooms, particularly in the Tempe and Phoenix West sub-markets. Although demand has increased, it has not quite kept up with the increase in supply resulting in slightly lower occupancy rates.

5.3 Visitor Profile

The typical visitor to Phoenix is about 42 years old with an average income of $60,800. The majority, 62 percent, are vacation travelers, while 38 percent come to Phoenix for conventions or business. Typically, visitors stay for 4.7 days, spending about $105 per day. The satisfaction rate is high with 80 percent of visitors planning to return on future trips.[29]

About one third of visitors are families, about 26 percent are couples, and an additional 28 percent are single adults. The largest segment, about 39 percent, stay in hotels, with the remainder staying in private homes and other accommodates. Most arrive by auto (55 percent) or by air (39 percent). Visitors are typically well educated with 44 percent having a college and/or graduate degree. Most work in managerial/professional positions or technical and sales occupations.[30]

Most visitors travel a significant distance with the average one-way mileage estimated at 653 miles. Almost 40 percent come from non-Western states, but the largest single state of origin is California, which accounts for 29 percent of tourists.[31]

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[26] Center for Business Research, Arizona State University, 1997.
[27] Greater Phoenix Convention and Visitors Bureau, 2000.
[28] Warnick and Company, Smith Travel Research, 1999.
[29] Arizona Hospitality and Resource Center, Northern Arizona University, 1999.
[30] D.K. Shifflet and Associates, 1999.
[31] D.K. Shifflet and Associates, 1999.

5.4 Projections

According to the Travel Industry Association Foundation, employment in the tourism sector was projected to grow by 18 percent nationally from 1994 to 2005. This is in contrast to a projected 10 percent increase in construction and a 7 percent decline in manufacturing employment during the same time period.[32]

In the short term, Arthur Andersen's Hospitality and Leisure Services group in Phoenix predicts that the decline in occupancy and average daily room rates that occurred in 1999 and 2000 due to supply outpacing demand will turn around in 2001 with a positive outlook projected for the local tourism industry.[33]

5.5 Tourism Industry Trends

A number of national trends in the tourism industry can be identified that will shape the future of travel and will affect the magnitude of impacts on local communities.

Technological Changes. More people are accessing travel information and purchasing travel on the Internet. Although this will eliminate intermediaries, it allows for more sophisticated targeted marketing to special interest groups. As people become more technologically dependent, the ability to maintain electronic communications via the Internet and cell phones will also become an important feature for travel destinations.[34]

Higher Expectations. As our society becomes more and more busy, people will expect to maximize their enjoyment from leisure and vacation time. High quality personal service, accommodation of diversity, and family-oriented travel will be essential factors for top performing destinations. Travelers will also place a higher value on timesaving conveniences such as pre-purchased tickets and quicker check in/check out so that more time can be devoted to actual leisure activities.[35]

Short Trips. Weekend vacations will continue to increase in popularity and will partially replace one to two week family vacations of the past.[36] These short trips are typically booked only one to two weeks in advance, often via the Internet.

Family-Orientation. As more families fall into the sandwich generation, destinations that offer accommodations and activities for multi-generational families will become more popular. Family vacations may also shift somewhat away from an exclusive summer activity as more states institute year-round school schedules with shorter breaks throughout the year.

Increased Diversity. As the Hispanic population grows and becomes a major portion of the consumer market, destinations that feature attractions targeting the Hispanic market will have a competitive advantage.[37]

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[32] Arizona Tourism Alliance, 1999.

[33] Hague, Al and Dan Nahom, "Arizona's Millennium: The Rising of Phoenix." Winter 1999/2000.

[34] Heffernon, Rick. "Destination Flagstaff: How Important is the Flagstaff-Area Tourism Cluster?" Morrison Institute for Public Policy. January 2000.

[35] Heffernon, Rick, January 2000.

[36] Leones, Julie. "Tourism Trends and Rural Economic Impacts." University of Arizona Department of Ag and Resource Economics, 1995.

[37] Heffernon, Rick, January 2000.

Eco-Tourism and Educational Travel. All types of travelers, but particularly seniors and early retirees will generate increasing demand for educational tourism, nature experiences, agricultural tourism and heritage or cultural tourism.[38]

Shopping Attractions. Shopping will continue to be an important feature of destination tourism. In particular, locally made unique goods will become increasingly popular.[39] In addition, shopping areas that offer a wide range of products and services to keep visitors at their outlets longer will benefit from increased sales.[40]

Attraction of Vacation Ownership. Destinations that offer hotel and motel accommodations along with opportunities for visitors to purchase condominiums and timeshare will increase in popularity.[41]

There are some additional trends and barriers that are affecting Arizona, and in particular Maricopa County's tourism industry.

Increased Competition. Arizona is facing increased competition for tourism dollars, particularly from Las Vegas. Arizona's share of the travel market declined by 0.5 percent in 1999/2000. Nevada is spending $160 million per year to attract visitors for golf and gaming, compared to only $8.6 million spent in Arizona. Private funding from the hospitality industry for more aggressive marketing may become necessary to keep up with the competition. Also, the development of four and five star resorts with casinos on Indian reservations will help Greater Phoenix compete with Las Vegas.

Adequacy of Convention Facilities. While the City of Phoenix has seen a rebirth of its downtown core, the Phoenix Civic Plaza is falling behind other major cities as a convention center. The facilities need to be expanded and renovated in order to keep pace. However, a very limited amount land is available for expansion in the area surrounding the Civic Plaza.[42]

Availability of Downtown Lodging. Another issue that goes hand-in-hand with the convention facilities is the availability of nearby hotel facilities. There are only 1,600 rooms within a five-block radius of downtown. Convention attendees are forced to stay in hotels in other parts of town, creating a less desirable situation for large conventions. Two additional downtown hotels have been proposed that would add 1,000 more rooms, but they are being delayed by legal issues.

Stadium Impacts. On a positive note, the development of a new Cardinals football stadium in the East Valley and a new hockey arena in the West Valley will be a boost for tourism in the region. The football stadium will likely enable Greater Phoenix to attract another Super Bowl that would generate significant tourism spending.[43]

Increased Supply of Limited Service Hotels. Due to the recent construction boom in limited service or business class hotels, there is increased pressure on full-service hotels to compete by seeking out more convention and tour groups.[44]

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[38] Leones, Julie, 1995.
[39] Heffernon, Rick, January 2000.
[40] Leones, Julie, 1995.
[41] Hague Al and Dan Nahom, Winter 1999/2000
[42] Balzer, Stephanie, "State Tourism Report Notes Fewer Predictable Trends." *The Business Journal*. March 24, 2000.
[43] Hague Al and Dan Nahom, Winter 1999/2000.
[44] Balzer, Stephanie, March 2000.

5.6 Conclusions

Tourism in Arizona, and in Maricopa County in particular, clearly has a notable impact on state and tax local revenues. Most tourist activities including lodging, entertainment, dining out and shopping are subject to sales tax. While these activities only account for about 13 percent of general fund sales taxes collected by cities, they still represent a sizeable amount of local revenues that are being generated by people from outside the area.

National and local trends will require some adjustments in order to continue to meet the needs of the new millennium tourist and maintain the region's current market share of national tourist expenditures. However, Greater Phoenix' established reputation as a world class destination, and its large base of accommodations and attractions will continue to support a strong presence and positive outlook for this key industry cluster.